ZURICH

Weekly Macro and Markets View

21 May 2024

Highlights and View

Most of China's economic indicators for April were weak, with credit and property data disappointing in particular

Public support is urgently needed and has started be forthcoming following the latest Politburo meeting, with the government intending to buy excess housing inventory.

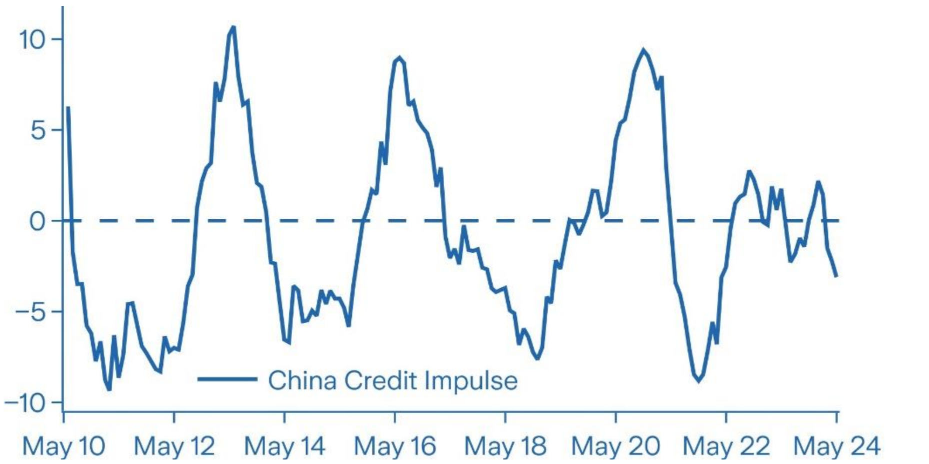
US inflation rates fall in April

The slowdown in price pressure is reassuring, but some service components are still on the rise.

US inflation data drive volatility in global government bond markets as investors reassess the near-term policy outlook

Bond yields appear to be fairly priced at current levels, but conditions are expected to remain volatile and dependent on inflation data.

China's April activity data broadly disappoint



Source: PBoC, Bloomberg (Note: 12 month net change of new lending increments over GDP increments)

We have been eagerly waiting for China's April economic indicators as first quarter data were distorted due to the Lunar New Year effect. Unfortunately, however, April statistics have been mostly disappointing, particularly those reflecting credit and property market conditions. Broad credit growth slowed sharply to its weakest pace on record, and aggregate financing fell for the first time since 2005, with its 8.3% YoY growth rate marking a record low. Corporate and household loan demand softened markedly, with government and policy bank bond issuance remaining weak. This may explain the latest Politburo call for faster issuance of special sovereign and local government bonds as the credit impulse has turned more negative, as shown in the chart above. Meanwhile, property market activity remains depressed. Property sales value dropped more than 30% YoY, while floor space under construction remained subdued, down more than 10% YoY. The price fall of newly built residential homes accelerated to -3.5% YoY, and secondary home prices also continue to fall while land sales revenue hit an eight-year low, down 21% YoY. The government announced various policy measures to support the property market, including easing mortgage rules, and encouraged local governments to buy unsold commodity housing. Retail sales and fixed asset investment statistics disappointed as well, while industrial production benefitted from solid exports.

US

Inflation and growth are slowing

Inflation rates were marginally weaker than consensus expected in April, providing a boost to government bonds and equities. Both headline and core inflation slowed to a monthly rate of 0.3% from 0.4% in March. The annual rates receded to 3.4% for headline and 3.6% for core inflation. While we are still not out of the woods with regard to inflation, the deceleration was a welcome relief after a series of disappointing prints. Meanwhile, the Conference Board's leading index fell by 0.6% MoM, underlining the persisting headwinds to growth that continue to weigh on economic activity. Retail sales did not grow at all in April indicating that consumers are becoming more reluctant to spend as the outlook on the job market is weakening. Similarly, industrial production was flat, too, following a very modest uptick the month before. The housing market is also feeling the pressure, with building permits falling for the second month in a row and housing starts rebounding less than expected following the significant dip in March.

Eurozone

The week that wasn't

Mixed data trickled through during a quiet week for the Eurozone. In keeping with recent trends, the German ZEW sentiment survey increased across the board as optimism continued to pick up for the European and German economic outlook. Headline Eurozone industrial production for March appeared to confirm that picture, rising 0.6% on the month and above market expectations, but once Ireland's extremely volatile series is removed the overall number is actually disappointing. We have yet to see an improvement on the manufacturing side, but think the second half of the year is likely to see a mild bounce. One further and unexpected data point was the disappointing Q1 GDP print for the Netherlands. Due to a combination of falling net trade and inventory drawdown, GDP fell 0.1% on the quarter, significantly below broad expectations of a 0.3% rise. Meanwhile, consumption growth looked robust at 0.7% on the quarter, and a provisional coalition agreement has been reached following last November's elections.

Japan

The recession should end soon

Japan's GDP release for Q1 came in weaker than expected, with real GDP contracting by 2% on an annualised sequential basis on top of a contraction in the second half of last year. Private consumption, housing investment, capex and net exports all contributed to the downside. Negative real income growth remained a burden for households for the fourth quarter in a row, and the weak yen made imports more expensive while surging inbound tourism keeps lifting hotel and restaurant prices. The large drop in exports was to a good extent attributable to enforced factory shutdowns by an automaker as well as the Noto earthquake at the start of the year. On a positive note, public investment contributed positively to Q1 GDP, and we expect Japan's economy to pick up steam in Q2 and Q3, which should alleviate the pain for consumers and producers going forward. We do not expect another rate hike by the Bank of Japan before Q3.

Australia

Fiscal stimulus is significant

The Australian Government Budget for 2024/2025 projects a surplus of AUD 9.3 bn (0.3% of GDP) for the fiscal year 2023/2024, an improvement from the previous deficit forecast. However, the budget balance is expected to fall into deficit in the following four years, with net fiscal stimulus estimated to be around AUD 25bn. Income tax cuts and cost-of-living relief measures, including energy bill relief and rent assistance, are included in the budget. While these measures will technically lower inflation in the near term, tax cuts and increased public spending may add demand to the economy and risk keeping inflation higher for longer. The unemployment rate increased more than expected in April due to improved labour supply, but job growth remained strong at 2.8% YoY. Wage growth eased further in Q1, but we think the Reserve Bank of Australia will remain cautious and closely monitor the impact of forthcoming fiscal stimulus on consumer behaviour and inflation. We expect no rate cuts this year in Australia.

Bonds

Inflation data drive market volatility

A softer than expected US CPI print triggered a relief rally in global bond markets mid-week, though pricing partly retraced as concerns around sticky services inflation persist. This left the 10yr Treasury yield down 8bps on the week, and almost 30bps lower compared to the recent peak in April. Moves were largely led by the short end, with a November Fed rate cut fully priced, but with prospects for a September cut still limited. US data drove volatility in European bond markets as well, leaving yields flat or modestly down on the week. A June ECB rate cut is almost fully priced, with close to three cuts expected by year end. Gilt yields fell, with dovish comments from the BoE raising hopes of policy loosening in summer despite wage data remaining brisk. The odd one out was Japan, where yields rose with the 10yr yield now approaching 1%. At current levels, yields appear to be fairly priced in most regions, but pricing is likely to remain volatile, with the policy outlook still sensitive to news on inflation.

What to Watch

- In the UK, inflation data, retail sales, and the latest PMIs will provide important insights into the current state of the economy.
- The Bank of Korea and Bank Indonesia are expected to keep policy rates unchanged. In Japan, we will focus on PMIs and the Reuters Tankan for May as well as foreign trade and CPI data for April. India will release May PMIs. Malaysia's exports for April are likely to improve further. Singapore and Thailand will release GDP data for Q1. Taiwan and Singapore will publish April production data. Markets will be closed in Malaysia, Singapore and Thailand on Wednesday, in India and Indonesia on Thursday, and in Indonesia on Friday.
- Q1 growth data will be released in Chile with analysts projecting 2.5% YoY. We are anticipating a reduction of 50bps in the monetary policy rate from the Central Bank later in the week.

Disclaimer and cautionary statement

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